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Ref A03364

PRIME MINISTER

Public Services Pay in 1980-81: Transitional Problems
(E(80) 122)

BACKGROUND

1. This paper arises following discussion at the meeting on 16 October (E(80) 37th - item 1) and discusses two transitional problems in relating pay to cash limits.

Staging

2. In the past cash limits have been based on the salary level at the start of the financial year, with a provision for an addition for any pay settlements in that year. Thus managements - both central government and elsewhere in the public sector - have found it convenient, when faced with reconciling large pay rises with cash limits, to stage the payments, so that the average pay in the year concerned is kept within the cash limit provision, but leaving the full salary level to be paid near the end of the financial year, so that this higher level is carried into the base for the next year's cash limit. This means an increase in the paybill between the two financial years which can be well in excess of the cash limit provision. The staff who are affected by staging suffer a loss of salary in the first of the years, since their average pay is lower. But they have been willing to acquiesce in the arrangement, because what they believe to be the "right" salary is eventually paid. Clearly this arrangement dilutes the discipline of cash limits over pay settlements, and the Chancellor proposed in E(80) 118 that staging should not be used in the future. Instead the base for the new cash limits should be taken as the average, rather than the final, salary level in the preceding year.

3. The paper discusses three groups which had staged settlements last year, and questions whether it would be practicable to start the new system immediately, which would reduce the entitlement of these groups to any "standard" increase in pay provision in the new cash limits.

4. Annex A discusses possible options. The Chancellor has decided to recommend making a special provision above cash limits for these groups this year, and starting with a clean sheet from then on, (with the proviso that his colleagues accept that the general "new pay" factor will be the tight one of 6%).

5. The teachers are in some respects a special case, because of the "Clegg error". But as you will be discussing in the paper on the Rate Support Grant settlement at Cabinet on Thursday, any abatement of teachers' salary provision would have to be distributed through the Rate Support Grant differentially between education authorities - which include all the shire counties and Outer London boroughs - as against other local authorities. It could thus seriously upset the political balance of the proposed Rate Support Grant distribution package.

Problems when pay year and cash limit year do not coincide

6. There are a number of groups whose pay is settled in the autumn, and whose settlements are therefore influenced by cash limit assumptions made almost a year before. Last year the cash limit assumption for settlements in the second of the pay rounds affecting 1980-81, ie settlements between August 1980 and March 1981, was 13% - 14%. If groups settling this autumn do so in single figures, there will be some spare provision in the cash limit for their pay. Alternatively there is the risk that their negotiators will not feel under a tight cash constraint. In theory it would be possible to reduce all these cash limits, to allow for the new standard pay provision. This would be the converse of the process last year of increasing cash limits, when the previous Administration's 5% assumptions proved unreasonable. There are, however, serious objections to adjusting cash limits once they are set, and although there is some excess pay provision, the cash limits concerned will have been subject to a squeeze because price movements have exceeded the original provision. The Chancellor therefore recommends no retrospective alteration, but merely that the 1981-82 cash limit should allow only for the new pay provision, (and would therefore be lower than the provision assumed for the closing months of 1980-81).

HANDLING

7. It seems unlikely that colleagues will disagree strongly with the Chancellor's recommendations (we already know that the Lord President of the Council and the Secretaries of State for Industry and Education will accept them). The main problem therefore is in bringing together the series of interlinked decisions which will be taken over the next few days. The Chancellor's recommendations today are conditional on a 6% new pay assumption, but you cannot reach a final decision on that until the full Cabinet consider his paper C(80) 60. As already noted above, the decisions on cash limit factors, and the treatment of staging, both interact with the Rate Support Grant distribution, which is also to be considered by Cabinet on Thursday.

8. You might ask the Chancellor of the Exchequer to introduce the paper, and then inquire whether any colleagues wish to dissent from his recommendation. If any wish to do so, it will probably be because they are worried about the "realism" of the 6% new pay figure. You will want to discourage such discussion - which is for Cabinet - and confine the present meeting to the principle of the way these anomalies should be handled, irrespective of the exact size of the new pay figure.

9. The Secretary of State for Defence has to leave the meeting early, and you might give him an early opportunity to speak. Apart from him, the main Ministers with an interest are the Lord President (who wrote to colleagues on the 22 October), the Secretary of State for Education and the Secretary of State for the Environment.

CONCLUSION

10. The conclusion will probably be that the Committee agree provisionally that the transitional problems should be handled in the manner recommended by the Chancellor in Option (a) of Annex A, and Option (b) of Annex B of the E(80) 122, subject to final confirmation when the "new pay" provision for cash limits is decided by Cabinet.

ROBERT ARMSTRONG

(approved by the Secretary of the Cabinet and signed on his behalf)

27 October 1980